THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM BEAUFORT COUNTY
Court of Common Pleas

Marvin S. Dukes, III, Special Circuit Court Judge for Beaufort County

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Case No. 2012-213239

Town of Hilton Head Island,.....Respondent,

v.

Kigre, Inc.,.....Appellant.

FINAL BRIEF OF APPELLANT

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

OTHER AUTHORITIES

STATEMENT OF ISSUES ON APPEAL

1. DID THE TRIAL COURT ERR IN FAILING TO FIND THE BUSINESS LICENSE FEE ORDINANCE VIOLATED THE DORMANT COMMERCE CLAUSE?

2. DID THE TRIAL COURT ERR IN FAILING TO FIND THE BUSINESS LICENSE FEE ORDINANCE VIOLATED THE EQUAL PROTECTION CLAUSES OF THE FEDERAL AND STATE CONSTITUTIONS?

3. DID THE TRIAL COURT ERR IN FAILING TO FIND THAT THE TOWN OF HILTON HEAD ISLAND FAILED TO FOLLOW ITS OWN ORDINANCE?

4. DID THE TRIAL COURT ERR IN FAILING TO HOLD THAT KIGRE HAD PAID ALL THAT IT WAS LIABLE FOR PAYING UNDER THE EXPRESS TERMS OF THE BUSINESS LICENSE FEE ORDINANCE?

5. DID THE TRIAL COURT ERR IN FAILING TO FIND THAT THE INCLUSION OF A PROVISION IN THE ORDINANCE ALLOWING RECOVERY OF ATTORNEYS FEES BY THE TOWN WITHOUT A SIMILAR PROVISION ALLOWING FOR RECOVERY OF ATTORNEYS FEES BY A DEFENDANT, IS A DENIAL OF THE EQUAL PROTECTION OF THE LAW?

6. DID THE TRIAL COURT ERR IN FAILING TO FIND THAT THE TOWN ORDINANCE WAS UNCONSTITUTIONALLY VAGUE AND THEREFORE UNENFORCEABLE?

STATEMENT OF THE CASE

On March 29, 2006, the Town of Hilton Head Island brought this action against Kigre, Inc., seeking an accounting as to Kigre's gross income for the years 2001, 2002, 2003, 2004 and 2005, and further seeking an award of damages and late fees for "business license fees" that had allegedly not been paid, totaling $41,645.81. The Town also sought a Declaratory Judgment that Kigre was "not entitled to any alleged Federal exemption shielding Kigre from paying the Town's business license fee." Kigre filed an

Answer and Counterclaim alleging that the Town's attempts to collect business license fees on Kigre's sales made outside of the state of South Carolina was violative of the Dormant Commerce Clause of the United States Constitution, raised other defenses and sought its own Declaratory Judgment that the ordinance was unconstitutional and was not being applied as enacted. A Reply was timely filed by the Town on October 10, 2006. Eleven months later, on August 30, 2007, based upon the Town's recognition that it had failed to provide Kigre with a required opportunity to appeal to the town council, the Town filed a Motion to Dismiss the entire action. That Motion was never argued nor ruled upon.

Due to health reasons, Kigre's original attorney withdrew from the case in 2009, and new counsel entered the case and filed an Amended Answer and Counterclaim on September 2, 2009, raising additional defenses and counterclaims.

The case was tried non-jury by Master In Equity and Special Circuit Judge Marvin H. Dukes, III, on December 8-9, 2010, and April 27, 2011. Judge Dukes filed his initial Order Ending Case on February 7, 2012, and Kigre filed its Motion to Alter or Amend Judgment on February 16, 2012, and Judge Dukes heard argument on the Motion on May 17, 2012. On September 20, 2012, Judge Dukes filed his Amended Order Ending Case. On October 16, 2012, Kigre filed its Notice of Appeal on the Town.

FACTS

Kigre, Inc. is a high tech manufacturer of laser components and laser glass, which

products are then shipped out-of-state and primarily used in the later manufacture of laser range finders and research systems for the military. (R. pp. 83-84) It is a family owned business, which opened on Hilton Head in 1986. (R. p. 84, line 5) Kigre's only manufacturing facility and principal place of business is in Hilton Head, and Kigre pays property and personal property taxes on it manufacturing facility to the Town of Hilton Head and Beaufort County. (R. pp. 83-85) During the time period here at issue, 2002-2006, Kigre sold more than 99.5 percent of the laser components and laser glass it manufactured on a yearly basis to out-of-state purchasers through interstate commerce. (R. p. 130, lines 10-23) The Town does not dispute that percentage of out-of-state sales. (R. pp. 117, line 22-118, line 10)

The Town of Hilton Head Island enacted a Business License Ordinance in 1983, known as Ordinance 10-1-10 et. seq. (R. p. 153) The salient portions of the Ordinance as it existed in 2006 relating directly to this appeal are:

> Section 10-1-10. License Required.
>
> Every person engaged or intending to engage in any calling, business, occupation or profession listed in the rate classification index portion of this chapter, in whole or in part, within the limits of the town, is required to pay an annual license as hereinafter provided.
>
> Section 10-1-20. Definitions.
>
> (2) Classification: That division of businesses by major groups subject to the same license rate, as determined by a calculated index of ability to pay based on national averages, benefits, equalization of tax burden, relationship of services, or other basis deemed appropriate by the town council.
>
> (3) Gross income: The total revenue of a business, received or accrued, for one fiscal year collected or to be collected by reason of the conduct of business within the town, excepting therefrom income from

business done wholly outside of the town on which a license tax is paid to some other municipality or a county and fully reported to the town. Gross income from interstate commerce shall be included in the gross income for every business subject to a business license fee. The gross income for business license purposes shall conform to the gross income reported to the Internal Revenue Service, the South Carolina Department of Revenue and Taxation, or the South Carolina Insurance Commission.

Section 10-1-30. Purpose and duration.

The business license levied by this chapter is for the purpose of providing such regulation as may be required by the businesses subject thereto and for the purpose of raising revenue for the general fund through a privilege fee....

Section 10-1-60. Deductions and exemptions.

No deductions from gross income shall be made except from income from business done wholly outside of the town on which a license tax is paid to some other municipality or a county, or income which cannot be taxed pursuant to state law. The applicant shall have the burden to establish the right to a deduction by satisfactory records and proof....The license inspector shall determine the appropriate classification for each business. No person shall be exempt from this chapter by reason of the payment of any other tax, unless exempted by state law, and no person shall be relieved of the liability for the payment of any other tax by reason of the application of this chapter.

Section 10-1-100. Inspections and audits.

For the purposes of enforcing the provisions of this chapter the license inspector or other authorized agent of the town is empowered to enter upon the premises of any person subject to this chapter to make inspections, examine and audit books and records, and is shall be unlawful for any person to fail or refuse to make available the necessary books and records during normal business hours with twenty four (24) hours' prior written notice. (Remainder of Section 10-1-100 omitted for brevity, but is set forth in Plaintiff's Exhibit 12, R. p. 155.)

Section 10-1-110. Assessments.

When any person shall have failed to obtain a business license or to furnish the information required by this chapter or the license inspector, the license inspector shall proceed to examine the records of the business or other available records as may be appropriate and to conduct investigations and statistical surveys as he may deem appropriate to assess a license tax and penalties as provided herein. A notice of assessment shall be served by

certified mail and an application for adjustment of the assessment may be made to the license inspector with fine (5) days after the notice is mailed or the assessment will become final. The license inspector shall establish by regulation the procedure for hearing an application for adjustment of assessment and issuing a notice of final assessment. A final assessment may be appealed to town council only by payment in full of the assessment under protest within five (5) days and filing of written notice of appeal within ten (10) days after payment pursuant to provisions of this chapter relating to appeals to town council.

Section 10-1-160. Appeals to town council.

(a) Any person aggrieved by a final assessment or a denial of a business license by the license inspector may appeal the decision to town council by written request stating the reasons therefor filed with the town clerk within ten (10) days after the payment of the assessment under protest or notice of denial is received.

(b) An appeal or a hearing on revocation shall be held by town council with thirty (30) days after receipt of a request for appeal or service of a notice of suspension at a regular or special meeting of which the applicant or licensee has been given written notice. At the hearing all parties shall have the right to be represented by counsel, to present testimony and evidence and to cross examine witnesses. The proceedings shall be recorded and transcribed at the expense of the party so requesting. The rules of evidence and procedure prescribed by the town council shall govern the hearing. Town council shall by majority vote of members present render a written decision based on findings of fact and the application of the standards herein which shall be served upon all parties or their representatives and shall be final unless appealed to a court of competent jurisdiction with ten (10) days after service.

Section 10-1-190. Classification rates, schedules.

The license fee for each class of business shall be computed in accordance with the following rates and with the Standard Industrial Classification (SIC) Manual 1987, except in cases of conflict between the provisions of the SIC and Town Code, the Town Code provisions shall prevail. (Classifications omitted for brevity, but are set forth in Plaintiff's Exhibit 12, R. pp. 164-190.)

Section 10-1-200 Local Industry License.

Any person who desires to exclusively engage in the business of offering for public sale at designated locations, as determined by the town manager, farm and garden products or flowers grown of the property of such

> person, or flower arrangements, arts or crafts produced in the home of such person, or seafood caught by such person, shall secure from the town an annual business license, but shall be exempt from the payment of a business license fee.

From the time Kigre opened its manufacturing operation in 1986 until 2004, Kigre had annually submitted a business license fee application to the Town comporting with the time requirements of the ordinance, and paid the minimum fee due, which was $62.50 annually. (R. p. 89) (Jeffrey Myers, Kigre's Vice President and Chief Operating Officer) (R. p. 127) See Defendant's Exhibit 10, the Kigre business license application from 1994, which is the earliest dated application the Town produced under subpoena. (R. p. 151)

Mr. Myers paid the minimum $62.50 because he took the position that the gross income of Kigre, which was 99.5 percent made up of interstate and international sales, was not subject to a "sales tax" being imposed by the town. (R. p. 89, line 25 – p. 90, line 4) The Town accepted the minimum annual payments from Kigre for approximately 18 years, until 2004, when Mr. Myers received a letter from the town advising him that Kigre had been "randomly selected" for a verification of gross income for the years 2001-2003. See Plaintiff's Exhibit 5. (R. p. 146) That letter, from Deputy Finance Director Steven Markiw, requested that Kigre send to the Town copies of Kigre's 2001, 2002 and 2003 Federal Income Tax Returns. In reply, Mr. Myers sent Markiw an email stating "As we (Kigre) do not have any revenue generated from sales inside the state of South Carolina, all of our revenue is exempted from the sales tax under the US Federal laws." See Plaintiff's Exhibit 6. (R. p. 147)

The Town responded two weeks later, on April 6, 2004, telling Kigre that the

business license fee was not a sales tax, but a "privilege of doing business" excise tax, citing the South Carolina Municipal Association's Business License Handbook, and again requested that that Kigre turn over the tax returns. "Should you choose not to comply with the request the Town will have no choice but to begin proceedings to suspend your license. " See Plaintiff's Exhibit 7. (R. p. 148)

Two days later, on April 8, 2004, Mr. Myers advised Mr. Markiw by email that "[i]f we are going to go through with this, let's do it according to the law." Referring to Markiw's threat to "begin proceedings to suspend your license", Myers correctly noted that "the town has no legal authority to take such actions at this time:"

> There is nothing in the Town Code that requires Kigre to submit anything to the Town by April 23, 2004 (Section 10-1-100). The Town may request an audit on 24 hours notice. To date, the Town has not scheduled any appointment to review our records. We will be glad to have a Town representative visit our facility. We will allow the Town inspector to examine any pertinent documents requested. In the Town's discretion, it may; then assess additional taxes (Please note that even the ordinances call it a "License Tax"). This will be paid immediately under protest. At that time we will make a written appeal to the Town Council. Town Council is then required to hear the appeal within with 30 days in an open meeting. During this appeal, we intend to give a complete defense. This will include relevant case law and the statements made by an expert at the SC Dept of Revenue that the code as written will be struck down in Federal Court. See Plaintiff's Exhibit 9. (R. p. 150)

After Mr. Myer's email of April 8, 2004 quoted above, Kigre heard nothing further from the Town in 2004. (R. p. 100, lines 16 – 22) In 2005, Kigre submitted its business license fee application, paying the minimum again, and was issued a business license by the Town. See Plaintiff's Exhibit 10. (R. p. 151)

Then, 16 months later, in August 2005, Mr. Markiw wrote another letter to Kigre

advising that Kigre had "been selected for a verification of gross income for the years 2002, 2003 and 2004" and requested copies of Kigre's 2001, 2002 and 2003 Federal Income Tax returns be sent the town in 14 days. See Plaintiff's Exhibit 11. (R. p. 152) Mr. Myers again told them that they did not have the authority to demand Kigre produce income tax returns to "float around town hall." Instead, he invited them to audit his records and when the town agreed, Mr. Myers scheduled the day "within a week or so." (R. p. 128, lines 13 -24) The Town then sent out an auditor and a town employee in September 2005 to review Kigre's records, and Mr. Myers provided them with everything they asked to see. (R. p. 102, line 4) The Town then went quiet again. (R. p. 102, lines 20 - 23) The "results" of the Town audit were not given to Kigre until five years later, approximately one month prior to trial of this action. (R. p. 102, lines 20 -23) What was given to Kigre was a lawsuit.

> I heard nothing else from the town until they filed suit. I was never given an assessment, any notification of assessment, any dollar amount, or anything. I think it was some months later, six months or so, that they came in and just filed suit. (Testimony of Myers, R. p. 129, lines 4 – 9) See original Complaint dated April 3, 2006. (R. p. 32)

Kigre then hired G. Richardson Wieters to defend the corporation and he filed an Answer and Counterclaim dated August 17, 2006. (R. p. 37) Thereafter, following negotiations between counsel for both sides, it was mutually agreed that Kigre would be given the opportunity to pay the total amount demanded in the Complaint ($41,645.81)(the amount allegedly derived from the "audit") under protest and pursuant to Business License Ordinance Section 10-1-160, be given the opportunity to present its

appeal to Town Council. (R. p. 131, lines 22 – 25, - p. 132, lines 2 – 8) Kigre tendered the $41,645.81 check to the Town, along with an appeal letter from Mr. Wieters. See the Affidavit of Town Deputy Director of Finance Steven Markiw filed with the Court on or about August 30, 2007, with the Plaintiff's Motion to Dismiss the action (marked as Defendant's Exhibit 3 (R. p. 291)), which noted that Kigre paid the $41,645.81 to the Town under protest on November 13, 2006 and requested a hearing pursuant to Section 10-1-160 on the same day. However, citing the requirement that an appeal hearing be held within 30 days, Mr. Markiw states on oath that "A hearing on Kigre, Inc's business license fee liability was not held within thirty (30) days as required by Section 10-1-160 of the Ordinances of the Town of Hilton Head Island. As a result, the Town of Hilton Head Island refunded the entire $41,645.81 of business license fees and penalties Kigre, Inc. paid under protest from the 2002, 2003, 2004 and 2005 tax periods on February 2, 2007." (See Paragraph 6 of Markiw Affidavit, (R. p. 292)). (See also the Wieters' letter of appeal marked as Defendant's Exhibit 4 (R. p. 293) and the Town's refund check, Defendant's Exhibit 5 (R. p. 298))

Mr. Markiw further stated on oath that as of August 24, 2007, Kigre "does not owe any business license fees or penalties for the 2002, 2003, 2004, or 2005 tax periods," Kigre's business license fee periods were "currently" not being audited and "[t]here are no outstanding business license fee assessments against Kigre, Inc." as of August 24, 2007. (See Paragraphs 7, 9 and 10 of Defendant's Exhibit 3 (R. p. 292))

The Markiw Affidavit quoted above was attached to the Plaintiff's Motion to

Dismiss dated August 30, 2007, wherein the Plaintiff Town of Hilton Head Island requested the Court dismiss its Complaint and Kigre's Counterclaims because the Town acknowledged waiving its right to seek the $41,645,81. (R. p. 49) Notwithstanding that Motion and the Markiw affidavit, the Town moved forward in December 2010 at trial in an attempt to recover that money. However, Judge Dukes ruled that the Town "waived the right to collect on the $41,645.81" and the Town having failed to appeal from that finding against it, the holding of waiver as to any claims for business license fees relating to 2002, 2003, 2004 or 2005, is the law of the case. (See Amended Order Ending Case (R. p. 31))

STANDARD OF REVIEW

This appeal involves both legal and equitable causes of action. When both legal and equitable causes of action are maintained in one suit, each must be analyzed separately according to its own identity as legal or equitable. Rushing v. McKinney, 370 S.C 280, 633 S.E2d 917 (2006). In an action at law, on appeal of a case tried without a jury, the findings of fact of the Master will not be disturbed upon appeal unless found to be without evidence which reasonably supports the Master's findings. Townes Assocs. v. City of Greenville, 266 S.C. 81, 86, 221 S.E.2d 773, 775 (1976). In an action in equity, tried by the Master alone, without a reference (as here), the appellate court has jurisdiction to find facts in accordance with its views of the preponderance of the evidence. Id.

ARGUMENTS

1. THE TRIAL COURT ERRED IN FAILING TO FIND THE BUSINESS LICENSE FEE ORDINANCE VIOLATED THE DORMANT COMMERCE CLAUSE.

The Town Ordinance, specifically Section 10-1-20, includes gross income from interstate commerce sales in the computation of the business license fee due the Town: "Gross income from interstate commerce shall be included in the gross income for every business subject to a business license fee." Kigre's manufacturing sales from 2002-2006 were over 99.5 percent made in states beyond South Carolina and internationally. To acknowledge the less than one half of one percent of sales made in the jurisdiction of the Town or the State of South Carolina, Kigre has always agreed to pay the minimum business fee license computed by the Ordinance, and the Town does not contend that the minimum fee paid does not comport with those local sales.

The Commerce Clause of the United States Constitution provides that Congress has the power to regulate commerce among the several states. U.S. Const., Art. I, Section 8, cl. 3. However, the Commerce Clause is more than an affirmative grant of power; it has a negative sweep as well. Travelscape, LLC v. South Carolina Department of Revenue, 391 S.C. 89, 705 S.E.2d 28 (2012), *citing* Quill Corp. v. North Dakota, 504 U.S. 298, 309, 112 S.Ct. 1904, 1911, 119 L.Ed.2d 91 (1992). Even in the absence of Congressional regulation, the negative implications of the Commerce Clause, often referred to as the "Dormant Commerce Clause," prohibit state action that unduly burdens

interstate commerce. Travelscape, id. at 104, *citing* General Motors Corp. v. Tracy, 519 U.S. 278, 287, 117 S.CT. 811, 818, 136 L.Ed.2d 761 (1997). A state tax withstands a Dormant Commerce Clause challenge so long as the tax:

1. Is applied to an activity with a substantial nexus with the taxing state;
2. Is fairly apportioned;
3. Does not discriminate against interstate commerce, and,
4. Is fairly related to the services provided by the state.

See Complete Auto Transit, Inc. v. Brady, Chairman, Mississippi Tax Commission, 430 U.S. 274, 97 S.Ct 1076, 51 L.Ed.2d 326.

The Business Fee Ordinance is facially invalid in that it fails to apportion the amount of gross income made by a manufacturing business such as Kigre through its interstate sales. The Town sought to avoid the holding of Complete Auto by inserting a provision within the Ordinance providing that if (and only if) other states or taxing jurisdictions, levy other business license fees or similar taxes upon the interstate sales, then (and only then) will the Town of Hilton Head Island, apportion the sales of a business like Kigre: "No deductions from gross income shall be made except from income from business done wholly outside of the town on which a license tax is paid to some other municipality or a county...." Ordinance 10-1-60. (R. p. 154) Unfortunately, the Complete Auto holding and its progeny do not provide for such overreaching taxation. They provide that a manufacturer's interstate sales must be appropriately apportioned in all cases, not just where more than one jurisdiction levies such a tax.

The purpose behind the apportionment requirement is to ensure that each state taxes only its fair share of an interstate transaction. Travelscape, id., at 107. A tax is fairly apportioned if it is internally and externally consistent. Goldberg v. Sweet, 488 U.S. 252, 260-61, 109 S.Ct. 582, 588, 102 L.Ed. 2d 607 (1989). To be internally consistent, a tax must be structured so that if every State were to impose an identical tax, no multiple taxation would result. Id. at 261. The external consistency test asks whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed. Assuming that this Court may find the "reduction if another jurisdiction taxes" provision meets the prohibition on multiple taxation and therefore satisfies the internal consistency test, the external consistency test is still fatal to the Town's ordinance.

The external consistency test is really a test of fairness. Examining the manufacturing activities of Kigre under the external consistency test requires an analysis of what portion of the revenues from Kigre's interstate sales would reasonably reflect the in-state component of the value of the products produced on Hilton Head. In other words, manufacturing inherently creates a product where it is produced that has some value. But when it can't be sold in-state, it must (at a cost) be transported out-of-state for sale. These transportation and other associated costs that are an inherent part of interstate sales, have been the foundation of the U.S. Supreme Court's rulings prohibiting taxes that unfairly discriminate against interstate commerce.

This well-known and recognized fact regarding manufactured items intended for

out-of-state sale is specifically addressed in the South Carolina Municipal Association Handbook relied on by the Town of Hilton Head Island and entered into evidence by Kigre. (See Defendant's Exhibit 2) (R. p. 205) In providing guidance as to how to handle interstate commerce in the Business License Fee arena, the SCMA Handbook specifically notes: :[T]he tax may be levied only if all four tests in the Complete Auto Transit case are met." (R. p. 246) The Handbook then goes on to specifically address Manufacturing:

> "Manufacturing of goods intended to be shipped across state lines is not interstate commerce. Interstate commerce does not commence until the goods are shipped. **However, the activity of manufacturing produces no gross income as a general rule, and a business license must be computed on gross income from an activity subject to the privilege tax. A sale in interstate commerce may be a separate activity from the manufacture of the goods. Therefore, there must be an apportionment of the sales price to the manufacturing process conducted within the taxing jurisdiction.** (Emphasis added.) A tax on the capital invested in a business is no longer authorized by state law." SCMA Handbook (R. p. 247)

The Town acknowledges the Handbook is "[a] guidebook we use in doing our enforcement." (R. p. 113, lines 6 - 7) The Handbook's directive concerning the necessity of apportioning the manufacturing costs of products produced by Kigre for out-of-state sales is clear, concise and totally ignored by the Town of Hilton Head Island.

Steven Markiw, the Town Deputy Director of Finance, who was the Business License Fee administrator between 2002 and 2006, testified that "[W]e believe interstate commerce is not an exemption. We will adjust the necessary license fee with another municipality in another state or another county, but we do not regulate their business license regarding the portion of interstate." (R. p. 114, lines 19 – 24)

One exchange is particularly telling:

Question:	The Town of Hilton Head simply doesn't care to know whether or not Kigre's manufacturing is sold in the State of South Carolina or outside the State of South Carolina, right?
Markiw:	I would agree.
Question:	Your position is that they are liable for all of their sales:
Markiw:	Yes.
Question:	And the Town does not make any effort with anyone, Kigre or any other business, to apportion any type of tax if that entity maintains that its sales are out-of-state; is that correct?
Markiw:	That's correct.

(R. p. 114, line 25 – p. 115, line 15)

The Town's Ordinance violates the Complete Auto apportionment test on its face by stating that gross sales from interstate commerce are to be included in calculations for the business license fee. The Town's administrator for enforcement admits that the Town's policy was to "just say no" to any requests from a manufacturer such as Kigre to have its gross revenues apportioned for interstate sales. The Ordinance and its enforcement being in direct contravention of the Complete Auto requirement of fair apportionment of a tax based upon the revenue generated in the taxing state, the Ordinance must be struck down as a violation of the prohibition against taxes on interstate commerce.

In addition, the Town Business License Fee Ordinance violates the forth prong of the Complete Auto test in that the Town makes absolutely no effort whatsoever to correlate the tax to services provided by the Town. As the U.S. Supreme Court held in Commonwealth Edison Co. v. Montana, 453 U.S. 609, 627, 101 S.Ct.2946, 2958, 69 L.Ed.2d 884 (1981), the purpose of this test is to ensure that a State's tax burden is not

placed upon persons who do not benefit from services provided by the State.

Accepting the proposition that a tax/fee may be found to pass the test by showing that a business receives police and fire protection, the use of public roads and other advantages of civilized society, as was articulated by the U.S. Supreme Court in Goldberg v. Sweet, 488 U.S. 252, 267, 109 S.Ct. 582, 102 L.Ed. 2d 607 (1989), Kigre still contends that a good faith showing of an effort by the taxing body to monitor and evaluate a reasonable relationship between the tax/fee levied and the services provided, is required under the holdings of Commonwealth Edison, id., Goldberg, id., and their progeny. However, continuing the same type of interest shown by the Town's consideration of apportionment of income attributed to manufacturing that occurs within the Town's jurisdiction, Mr. Markiw testified that in regards to any routine analysis or evaluation of services and the tax, the Town simply doesn't care to make such:

Q. Does the town do anything to determine whether or not the business license fees levied upon businesses are in any way fairly related to the interest that the town provides?
A. No.
Q. The town makes no analysis on a yearly basis or a five year basis concerning the service that it provides to those businesses?
A. We analyze the service provided to all businesses during our budget process, but specifically related to how it relates to the business, the answer is no.
Q. A more appropriate question, the town really doesn't seek to analyze where the service in any way relates to the amount of money it gains from the business license fee on a yearly basis, correct?
A. We don't provide that analysis; no. The finance department's administrative position from the finance budgetary standpoint has not been done.
Q. All right. The town brings in, as I understand about 7.9 million a year in business license fees?
A. Correct.

Q. At least according to this year's number?
A. That's correct.
Q. Do you have testimony for this Court that will provide us any useful guidance on the amount of specific services the town provides for businesses?
A. No.

(R. p. 115, line 16 – p. 116, line 25)

The Town's counsel attempted to rehabilitate the witness on redirect and Kigre again acknowledges that the Town provides certain services, such as police, fire and EMS, that would respond to Kigre's business in the event of emergency. However, Kigre asserts that under the Complete Auto test, a good faith showing of some effort to balance the services rendered to businesses with the tax/fees charged to a company that sells 99.5 percent of its products in interstate commerce is required.

2. THE TRIAL COURT ERRED IN FAILING TO FIND THE BUSINESS LICENSE FEE ORDINANCE VIOLATED THE EQUAL PROTECTION CLAUSES OF THE FEDERAL AND STATE CONSTITUTIONS.

The Town of Hilton Head Island Business License Fee Ordinance contains a provision that waives any fee from certain businesses, with the decision of waiver left solely to the Town Manager without any reasonable guidelines or parameters. This provision, Section 10-1-200 (R. p. 190), states as follows:

> Section 10-1-200 Local Industry License.
>
> Any person who desires to exclusively engage in the business of offering for public sale at designated locations, **as determined by the town manager**, farm and garden products or flowers grown of the property of such person, or flower arrangements, arts or crafts produced in the home of such person, or seafood caught by such person, shall secure from the town an annual business license, but shall be exempt from the payment of a business

license fee. (Emphasis added)

This provision, allowing for the complete exemption of payment of a business license fee by an undefined and unknown class of individuals, denies Kigre, Inc. and all other businesses and individuals similarly situated, the equal protection of the law. The Business License Fee Ordinance requires payment of a Business License Fee by all other similarly situated persons or businesses conducting similar operations. See the following non-exempted Standard Industrial Classification Manual rate classifications in the Ordinance, Plaintiff's Exhibit 12 (R. p. 153): Class 5999 "Promoter/Coordinator of Arts and Crafts Shows" (R. p. 161); Class 53 "General Merchandise Stores" (R. p. 164); Class 01 "Agricultural production—Crops" (R. p. 166); Class 02 "Agricultural production—Animals" (R. p. 166); Class 20 "Food and kindred products" (R. p. 166); Class 09 "Fishing, hunting and trapping" (R. p. 166).

The Equal Protection Clauses of our federal and state constitutions declare that no person shall be denied the equal protection of the laws. U.S. Constitution, Amendment XIV, Section 1; S.C. Constitution, Article I, Section 3. "This simply means that no person, or class of persons, shall be denied the same protection of the laws which is enjoyed by other persons or other classes in the same place and under like circumstances." City of Beaufort v. Holcombe, 369 S.C. 643, 648, 632 S.E.2d 894 (2006), *citing* Harrison v. Caudle, 141 S.C. 407, 416, 139 S.E. 842, 845 (1927).

In evaluating whether an enactment affords equal protection, the Court must first decide what level of scrutiny to apply. In re Luckabaugh, 351 S.C. 122, 147, 568 S.E.2d

338, 351 (2002). Our courts generally analyze equal protection challenges under one of three standards: (1) rational basis; (2) intermediate scrutiny; or, (3) strict scrutiny. See City of Beaufort v. Holcome, 369 S.C. at p. 648 and cases cited therein. If the classification does not implicate a suspect class or abridge a fundamental right, the rational basis test is used. Denene, Inc. v. City of Charleston, 359 S.C. 85, 91, 596 S.E.2d 917, 920 (2004). Inherently suspect classifications include those based on factors such a "race, religion or alienage." Sunset Cay, LLC v. City of Folly Beach, 357 S.C. 414, 429, 593 S.E.2d 462, 469 (2004).

In this case, the businesses singled out for unfair exemption from the fee are not facially "suspect" classes of business, and thus it would be appropriate to use the "rational basis" test. To satisfy the equal protection clause under the rational basis test, a classification must (1) bear a reasonable relation to the legislative purpose sought to be achieved, (2) members of the class must be treated alike under similar circumstances, and (3) the classification must rest on some rational basis. Sunset Cay, 357 S.C. at 428, 593 S.E.2d at 469.So the question for this Court's consideration is whether there is a rational basis for the *complete exemption* of certain individuals and businesses based solely upon the Town Manager's potentially arbitrary opinions, from payment of any business license fee while all other businesses engaged in similar economic activities are forced to pay a business license fee.

Kigre's Chief Executive Officer Jeffrey Myers testified that the Ordinance as written and the Town's selective enforcement, result in discriminatory treatment to

businesses. "They are charging some people business licenses and not charging others. Some of them according to the law and some them not according to the law." (R. p. 101, lines 13 – 18)

> "The thing is that every single area they don't charge some native island businesses and they do others. They don't charge some schools, they do others. They don't charge some non-profits, they do others. They charge some plantations, they don't charge others. And it's all depending on, oh, who's our friend, who has votes, who doesn't have votes. It's ridiculous."
>
> Testimony of Jeffrey Myers, (R. p. 103, lines 6 – 18)

The Town admitted to this selective enforcement. Mr. Markiw, the person charged with the responsibility of enforcing the Ordinance, acknowledged that his finance office was well-aware of a number of businesses on Hilton Head set up to sell farm and garden products, flowers, flower arrangements, arts and crafts, and seafood, yet in the 27 years since the Business License Fee Ordinance had been enacted, not a single application for a business fee license had ever been made by one of them: "Now Mr. Markiw, has there ever been an instance since you've been in the finance department where there has been an application for such a business license?" Answer: "I don't believe so, no." (R. p. 110, line 22 – p. 111, line 2)

Mr. Markiw went on to admit (over objection) that he was personally aware of at least one instance where there was an on-going farmers market that would require a business license (with no payment) operating routinely, but then stated that "due to staffing constraints, we can't get to all of the businesses and we're doing that right now." (R. p. 111, line 19 – p. 112, line 18) Kigre acknowledges that the Equal Protection

clauses are subject to a wide scope of discretion and legislative enactments are to be avoided only when they are without any reasonable basis. City of Beaufort, 369 S.C. at 649. A municipal ordinance is a legislative enactment and is presumed to be constitutional. The burden is upon Kigre to prove the unconstitutionality beyond a reasonable doubt. Id.

The Business License Fee Ordinance as written and its complete exemption for certain businesses to be determined on an apparent case-by-case basis by the Town Manager, is plainly arbitrary and violates Kigre's equal protection rights. The admitted discriminatory application of the Business Fee License likewise violates Kigre's equal protection rights. There is no evidence in the record whatsoever that would support a "rational basis" argument for this exemption "of some but not of others". As opposed to the City of Beaufort holding where this Court found that an exemption of a class of business owners from payment of a business license fee on renting their own property to themselves was appropriate because the exempted businesses were actually paying a business license fee on the business that they were operating, here, the Town Ordinance arbitrarily exempts an entire class of businesses from paying any type of business license fee, while at the same time forcing all other businesses in the Town of Hilton Head to pay a tax.

3. THE TRIAL COURT ERRED IN FAILING TO HOLD THAT THE TOWN OF HILTON HEAD ISLAND IS NOT FOLLOWING THE BUSINESS LICENSE FEE ORDINANCE AS WRITTEN AND THUS SHOULD BE BARRED FROM ENFORCING SAME.

Section 10-1-20 of the Town's Ordinance establishes certain "Classifications" for different Town businesses, with each classification then being taxed at a different rate. Specifically, the "classification" of businesses for business license fee taxation purposes is set forth as follows:

> That division of businesses by major groups subject to the same license rate, as determined by a calculated index of ability to pay based on national averages, benefits, equalization of tax burden, relationship to services, or other basis deemed appropriate by the Town Council. (10-1-20(2)) (R. p. 153)

The undisputed facts adduced at trial show clearly that the Town makes no effort whatsoever to adhere to the single most important provision of its Ordinance: the classification of businesses "as determined by a calculated index of ability to pay." This is the linchpin in the Town's Ordinance and strict adherence, or at least a reasonable professional effort, to classify businesses according to their ability to pay as required by the Ordinance, is rightfully demanded by Kigre as a citizen taxpayer. Incredibly, the Town does not even make what can be construed as a feeble effort. Instead, the Town relies upon a 27-year-old document, described to the Court at trial as the "Standard Industrial Classification" system, which is incorporated into the Ordinance. The Town has adopted no other basis as appropriate classification guidelines. (R. p. 104, line 24 – p. 105, line 4). And the Town has no interest in learning about any of its businesses' ability to pay so they might be appropriately classified:

Q. Mr. Markiw, what is the standard industrial code and how does it classify businesses?
A. The standard industry classification codes in business is based

upon the type of services provided.

Q. It has to your knowledge nothing to do with a business' probability (sic)(should read "profitability"), correct?

A. That's correct.

Q. And it has nothing to do to your knowledge with the business' ability to pay a business fee license or another tax of some sort, right?

A. That's correct.

Q. Thus is there anything to your knowledge that the town does to classify businesses based upon their ability to pay?

A. No.

Q. Is there any national average that the town ever looked at in order to evaluate for businesses or for business license fee purposes?

A. No.

Q. Are there IRS statistics available for a man with your background and experience where you can go and look at business' ability to pay?

A. I believe there are.

Q. But you don't do anything—excuse me—the town doesn't do anything like that insofar as its enforcement?

A. That is correct.

Q. The next thing supposedly that's in the classification is calculated by the ability to pay based on national average benefits? Does the town in any way enter to evaluate what benefits are provided to a business when it considers what rate classification to put it in?

A. No.

Q. The next thing is evaluation of tax. Does the town do anything to make any evaluation of businesses when it places them in a classification as to whether or not it is exempt of a tax burden?

A. No.

Q. The next premise is the relationship of services. Does the town do anything to evaluate service to a type of business before it puts them—

A. No.

Q. And we've already talked about it, there is no other basis that's been deemed appropriate by the town council, correct; to your knowledge?

A. To my knowledge, no.

Q. So insofar as the classification system is set forth, when it says that the division of business by major groups subject to the same license rate ability to pay based on national average equation of tax burden relationship of service or other deemed appropriate by town

council makes no effort whatsoever to find any of those factors when it places the---

A. That's correct.

(R. p. 106, line 14 – p. 109, line 4)

The Town relies upon the Standard Industrial Classification system that was originally set forth in its Ordinance at adoption in 1983. There was no evidence offered by the Town as to the basis or factual accuracy of any version of the Standard Industrial Classification system, much less the 27-year-old version used by the Town. (However, the Town did admit that it wants to move away from the SIC: "One of the things we are trying to do is move forward in the near future trying to get funding for SIC to NAICS, and in that process we will hire an outside firm to be determined and we will review the businesses and we will review their classification at that point in time when we review the rate structure, that sort of analysis is by the town, and we are plan on doing that. So the answer is no, to this date we have not. Be we do have it in our queue to get it done and have never been more forward in that direction. We hope to do that very soon." (R. p. 123, lines 7 – 15)

The Town's actual classification of businesses is performed by a Town clerk when an application comes in. (R. p. 122, lines 12 - 18) The Town believes that the SIC separates businesses into classifications based upon the type of services provided by the business. The Town does not believe the SIC divides businesses into classifications based on an ability to pay, and does nothing whatsoever to determine a business' ability to pay. The Town basically admits that it collects 7.9 million dollars in business license fees

annually from businesses that it has classified and collected different amounts from, with no reasonable basis for the different classifications and charges. (R. p. 116, lines 14 – 17)

The undisputed fact that the Town believes its outdated Standard Industrial Code is based on the type of services provided by the business is also of critical importance. Despite the fact the Town's Ordinance is based on the specific factors of a business' ability to pay based on national averages, benefits, equalization of tax burden, relationship of services or other basis deemed appropriate by Town Council (there never having been any other basis considered or enacted), as is set forth above, the Town has does not even consider those factors. But to add insult to injury, the Town has never made any attempt whatsoever to regularly review the placement of a business in a certain classification, which results in business license fees being charged based on no rational method of classification review. This can be likened factually to a County assessing a piece of property in 1987 at a given value, and then leaving that property at that value for taxing purposes for more than 25 years. In fact, this Court may take judicial notice that the profitability of certain businesses varies dramatically over the course of the years, probably to a greater degree than the value of real estate.

Mr. Markiw's admissions as to the complete lack of interest the Town maintains in following the requirements of its own Ordinance demand that this Court issue its Declaratory Judgment holding the enforcement of the Ordinance in abeyance until a reasonable and sound system of classifying businesses according to the stated factor of "ability to pay" is incorporated and used by the Town of Hilton Head. Anything less will

result in the Town simply continuing its admitted flagrant disregard of its own Ordinance requirements.

4. THE COURT ERRED IN FAILING TO HOLD THAT KIGRE HAD PAID ALL THAT IT WAS LIABLE FOR PAYING UNDER THE EXPRESS TERMS OF THE BUSINESS LICENSE ORDINANCE.

The Town came in to Court on December 8, 2010, seeking damages totaling $41, 645.81 for fees and penalties allegedly attributed to Kigre's earnings in 2002, 2003, 2004 and 2005. However, during the trial, based upon the overwhelming evidence that the Town had failed to properly notify Kigre of the "assessed amount" per Section 10-1-110, and the unimpeached testimony of former Mayor Tom Peeples that the Town had waived the $41,645.81 because it had failed to provide the appeal hearing required under Section 10-1-160, (R. p. 133 – p. 135), the Town moved to amend its pleadings to conform to the evidence and Judge Dukes allowed the amendment, thereby eliminating any continuing claim for damages. (R. p. 125 - 126) In addition, Mr. Myers testified that Kigre had paid the Town every cent due under the formula of the Business License Fee properly apportioned for the manufacturing process, and that testimony is uncontradicted in the record. Thus, the only appropriate holding based on the evidence presented and the pleadings as amended, was a finding that Kigre had paid all Business License Fees due and payable through 2006.

5. THE COURT ERRED IN FAILING TO FIND THAT THE INCLUSION OF A PROVISION IN THE ORDINANCE ALLOWING RECOVERY OF ATTORNEYS FEES BY THE TOWN IN AN COLLECTION ACTION

WITHOUT A SIMILAR PROVISION ALLOWING FOR RECOVERY OF ATTORNEYS FEES BY A BUSINESS DEFENDING ITS ACTIONS, IS A DENIAL OF THE EQUAL PROTECTION OF THE LAW.

Section 10-1-120 of the Ordinance provides that the Town may charge a business, in addition to the fees due under the Ordinance, penalties and "costs of collection." (R. p. 156)

The Fourteenth Amendment to the United States Constitution and Art. I, Section III, of the South Carolina Constitution, forbid denial by the State of equal protection of the laws. When the constitutionality of a statute or ordinance awarding attorneys fees is questioned as a violation of equal protection, a court must determine whether the municipal classification is rationally related to the object of the statute. See Bradley v. Hullander, 277 S.C. 327, 287 S.E.2d 140 (1982).

Our Supreme Court has held unconstitutional a similar statewide statute providing for the recovery of attorneys fees to successful plaintiffs in Southeastern Home Building & Refurbishing, Inc. v. V.F. Platt, Jr., 283 S.C. 602, 325 S.E.2d 328 (1985). There, as here, the classification of one of two similarly situated parties to allow for the recovery of attorneys fees, was held to reflect no rational relationship to a legitimate State (or Town of Hilton Head Island) goal. Authorizing fee awards to prevailing Defendants, as well as Plaintiffs, would not chill the Town's right to seek relief in Court. The provisions of Ordinance 10-1-120 allowing for attorneys fees under the "costs of collection" provision is an unconstitutional denial of equal protection to the Defendant Kigre, Inc.

The Town of Hilton Head Island initiated this collection action in March 2006

and has cost Kigre attorneys fees for more than six years of litigation, prior to walking away from its claims for damages at trial in December 2010 based upon the former Mayor's testimony, Mr. Markiw's Affidavit submitted in March 2007, the uncontradicted evidence that the Town had failed to properly follow its Ordinance in the required notification of Kigre as to the "assessment" from the audit in 2006, and the clear evidence the Town failed to provide Kigre with an appeal hearing after requiring Kigre to pay the $41,645.81 in 2007 as a ticket in to the appeal process.

Kigre respectfully requests this Court hold an implied award of attorneys' fees is appropriate under the Ordinance for a business that ultimately defends itself from the Town's failed attempts to collect alleged past due taxes, penalties and collection costs under the Business License Fee Ordinance. Had the Town withdrawn the claim for damages in March 2007 when it moved to dismiss its case because of the clear waiver in failing to give Kigre its appeal hearing, much needless judicial time and litigation costs in discovery as to the basis of the damages and amounts due could have been avoided. Because of the Town's baseless, continuing collection actions, Kigre respectfully requests this Court hold that the imposition of attorneys fees against the Town would be appropriate and remand the case to Judge Dukes for further proceedings and the taking of evidence.

6. THE COURT ERRED IN FAILING TO FIND THAT THE TOWN ORDINANCE WAS UNCONSTITUTIONALLY VAGUE AND THEREFORE UNENFORCEABLE BECAUSE IT FAILED TO PROVIDE ANY TYPE OF ACCURATE OR RELIABLE MEANS, METHOD OR PROCEDURES TO INSURE BUSINESSES WERE PROPERLY CLASSIFIED.

The Town admits that a clerk who opens the mail in the business license department assigns the business to an SIC classification based on how he or she reads the application. (R. p. 122, lines 12 – 18) The Town admits the Clerk simply refers to the Ordinance. Therefore, all business applications are left to the vagueness of the Ordinance and its 1983 SIC tables. A plain reading of the Ordinance by the Court will reveal that the categories are vague, overlapping and not reasonably or rationally divided. The Town has never had any type of notification system in place to advise a business of its classification or reason therefore. Therefore, all businesses are simply at the mercy of the clerk who opens the application and are subject to the interpretation he or she may put on the business application that day, without any further guidance or resource. This process contains so many opportunities for error and/or miscalculation that it is inherently unconstitutionally vague and unenforceable.

The Due Process Clause protects "against the exaction of obedience to a rule or standard which [is] so vague and indefinite as really to be no rule or standard at all". A.B. Small Co. v. American Sugar Refining Co., 267 U.S. 233, 45 S.Ct. 295, 297, 69 L.Ed. 589 (1925). The constitutional standard for vagueness is the practical criterion of fair notice to those to whom the law applies. Toussaint, M.D. v. State Board of Medical Examiners, 303 S.C. 316, 320, 400 S.E.2d 488 (1991). A law is unconstitutionally vague if it forbids or requires the doing of an act in terms so vague that men of common intelligence must necessarily guess as to its meaning and differ as to its application. Toussaint, 303 S.C. at 320.

As is noted above, using the Toussaint standard, a plain reading of the Rate Classification Index from 1983 (R. p. 164), shows classifications that are vague, overlapping and not reasonably or rationally divided. The Ordinance is so vague and the procedure used to "classify" businesses so unstructured, that Kigre is denied its due process rights by the Town's application and enforcement of the Ordinance as written.

CONCLUSION

For the reasons stated, this Court should reverse the judgment of the Master in Equity and Special Circuit Judge, and enter its Judgment in favor of the Defendant Kigre, Inc. on all Counterclaims.

Respectfully submitted,

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May 16th, 2013

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM BEAUFORT COUNTY
Court of Common Pleas

Marvin S. Dukes, III, Special Circuit Court Judge for Beaufort County

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Case No. 2012-213239

Town of Hilton Head Island,.....Respondent,

v.

Kigre, Inc.,.....Appellant.

CERTIFICATE OF COMPLIANCE WITH RULE 211(b)

Pursuant to SCACR 211, I certify that the Appellant's Final Brief and the Appellant's Final Reply Brief, comply with Rule 211(b).

May 16, 2013

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THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM BEAUFORT COUNTY
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Marvin S. Dukes, III, Special Circuit Court Judge for Beaufort County

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Case No. 2012-213239

Town of Hilton Head Island,..... Respondent,

v.

Kigre, Inc.,..... Appellant.

PROOF OF SERVICE

Pursuant to SCACR 211, I certify that I have served a copy of the Appellant's Final Brief and the Appellant's Final Reply Brief, on the Respondent Town of Hilton Head Island by depositing a copy of it in the United States Mail, first class postage prepaid, on May 16, 2013, addressed to its attorney of record, Gregory M. Alford, P.O. Drawer 8008, Hilton Head Island, SC 29938-8008.

May 16, 2013

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